

UNITED STATES BANKRUPTCY COURT  
DISTRICT OF MINNESOTA

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In re:

Case No. 04-32864-DDO

Chapter 7

James Harold Jutz  
Darleen Mary Jutz,

**RESPONSE TO DEBTORS'  
MOTION FOR LIEN AVOIDANCE**

Debtors.

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**I. INTRODUCTION**

On or about April 2, 2004, First Federal Bank, fsb (“First Federal”) served and filed a summons and complaint (the “Action”), as well as a notice of lis pendens, against James Jutz, Darlene Jutz, Jutz Farms, Inc., Jesse Jutz, and Johanna Jutz as defendants (collectively, “Defendants”). In the Action, First Federal claims that Defendants are in breach of promissory notes and guarantees, and have converted and/or fraudulently transferred assets securing debt to First Federal. First Federal therefore requested the ability to foreclose on certain property, replevy certain property, and impose a constructive trust on assets purchased with proceeds from the conversion and/or fraudulent transfer of assets. First Federal has not proceeded any further with respect to the Action since James and Darlene Jutz (“Debtors”) filed their bankruptcy petition.<sup>1</sup>

Debtors have since filed a motion to avoid First Federal’s lien in the following property (the “Property”):

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<sup>1</sup> As a side note, Jesse Jutz has also filed bankruptcy. That case is currently before Judge Kishel, Case No. 04-32867-GFK.

<b>Item</b>	<b>Scheduled Value</b>
Baler Square 3x3x8 4755 23000	\$24,000.00
Shop Tools	\$950.00
John Deere Drill 8350	\$1,500.00
Fax Machine	\$10.00

Debtors should not be able to exempt the above property because they do not have an interest in the property and First Federal's lien does not impair an exemption which Debtors would otherwise be entitled to.

## **II. ANALYSIS**

In order to avoid First Federal's lien in the property, Debtors must show that (1) they have an interest in the Property; (2) First Federal's liens impair an exemption which they would otherwise be entitled to; (3) that First Federal's liens are nonpossessory, nonpurchase-money security interests in the Property; and (4) that the Property is of the type that can be exempted under section 522(f)(2)(B) of the Bankruptcy Code. *In re Peters*, 60 B.R. 711, 715 (Bankr.D.Minn. 1986).

### **A. Debtor Does Not Have an Interest in the Property**

Property interests are created and defined by state law. *Butner v. United States*, 440 U.S. 48, 55, 99 S.Ct 914, 918, 59 L.Ed.2d 136, 141-42 (1979). Debtors admit that the Property is owned by Jutz Farms, Inc. ("Jutz Farms"). Debtors do not have the interest claimed under state law for two reasons. First, Debtors cannot claim an interest in property under section 550.37 of the Minnesota Statutes. Second, any interest Debtors may have in the Property may be subject to a constructive trust.

1. *Debtors cannot claim an interest in property under section 550.37 of the Minnesota Statutes*

In their memorandum in support of their motion for lien avoidance, Debtors assert that section 550.37 subd. 5 of the Minnesota Statutes permits them to selectively exempt the Property owned by Jutz Farms. The relevant portion of this statute states:

When a *debtor* is a *partnership of spouses* or a *partnership of natural persons* related to each other within the third degree of kindred according to the rules of civil law, for the purposes of this subdivision, the *partners* may elect to treat the assets of the *partnership* as assets of the individual *partners*.

MINN. STAT. § 550.37 subd. 5 (emphasis added). Debtors have misinterpreted section 550.37 in two ways.

The first flaw in Debtors' argument is that Jutz Farms is not in bankruptcy. As stated in the statute, only partners of a *debtor* may elect to treat the assets of the partnership as assets of the partners. This language should not be broadened to include nondebtors because exemption laws are to be strictly construed and nothing should be taken by implication.<sup>2</sup> *Temple v. Scott*, 3 Minn. 419, 3 Gil. 306 (1859).

Second, Jutz Farms is a corporation, not a partnership. As stated in the statute, only the partners of a *partnership* may elect to treat the assets of the partnership as assets of the partners. This language should be strictly construed to exclude corporations. *See id.* Because Jutz Farms is not a partnership and is not in bankruptcy, Debtors should not be permitted to utilize section 550.37 of the Minnesota Statutes to create an interest in Property.

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<sup>2</sup> Furthermore, section 550.366 of the Minnesota Statutes refers to the definition of family farm corporation in section 500.24 of the Minnesota Statutes. Section 500.24 separately defines Family farm corporation, Family farm trust, and Family farm partnership. MINN. STAT. 500.24 subd. 2. It is therefore apparent that if the legislature intended to include family farm corporations, section 550.37 would also have a reference to section 500.24.

2. *Any interest Debtors have in the Property may be subject to a constructive trust*

Generally, property obtained by tort is not property of a bankrupt's estate. *In re Flight Trans. Corp. Securities Litigation*, 730 F.2d 1128, 1136 (8th Cir. 1984) (citing *Nicklaus v. Bank of Russellville*, 336 F.2d 144, 146 - 47 (8th Cir. 1964) (other citations omitted))). Specifically, if debtor's conduct gives rise to the imposition of a constructive trust, and thus debtor only holds bare legal title to the property subject to a duty to reconvey the property to the rightful owner, then the bankruptcy estate holds the property subject to the same limitations. *Id.* Here, Debtors' pre-petition conduct may give rise to the imposition of a constructive trust.

As stated above, First Federal is in State Court seeking to impose a constructive trust on Debtors' assets based on the alleged conversion and/or fraudulent transfer of livestock, crops, equipment and proceeds, securing First Federal's loans. Furthermore, First Federal has filed a complaint objecting to Debtors' discharge for willfully and maliciously injuring First Federal by converting property. To the extent that the Property constitutes converted assets or the proceeds of converted assets, Debtors cannot claim the Property as exempt because the bankruptcy estate would hold the Property subject to a constructive trust. *See Id.* If the Court believes that Debtors may have an interest in the Property, First Federal respectfully requests the Court to reserve a determination on the exemption and lien avoidance claim affecting the Property until the conclusion of both the adversary proceeding regarding Debtors' discharge and the state court foreclosure and constructive trust litigation, for which relief from stay has been sought.

### **III. CONCLUSION**

Debtors do not have an interest in the Property to exempt under state law for two reasons. First, Debtors cannot claim an interest in property under section 550.37 of the Minnesota Statutes. Second, any interest Debtors may have in the property may be subject to a constructive trust. To the extent the Court finds Debtor to have an interest in the Property, First Federal respectfully requests that any determination regarding an exemption or lien avoidance be stayed until the conclusion of the dischargeability adversary proceeding and state court litigation.

Dated: August 30, 2004

MACKALL, CROUNSE & MOORE, PLC

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U.S. BANKRUPTCY COURT  
DISTRICT OF MINNESOTA

In Re:

Bky. Case No. 04-32864-DDO  
Chapter 7

James H. Jutz and Darleen M. Jutz,

Debtor.

UNSWORN DECLARATION  
FOR PROOF OF SERVICE

Amy J. Ditty, employed by Mackall, Crounse & Moore, attorney(s) licensed to practice law in this court, with office address of 1400 AT&T Tower, 901 Marquette Avenue, Minneapolis, MN 55402-2859, declares that on the date set forth below, I served the annexed **Response to Debtors' Motion for Lien Avoidance** upon each of the entities named below by mailing to each of them a copy thereof by enclosing same in an envelope with first class mail postage prepaid and depositing same in the post office at Minneapolis, Minnesota addressed to each of them as follows:

Office of the United States Trustee 1015 U.S. Courthouse 300 South Fourth Street Minneapolis, MN 55415	(Trustee) Paul W. Bucher P O Box 549 Rochester, MN 55903-0549
(Debtor) James H. Jutz and Darleen M. Jutz 64644 – 300 <sup>th</sup> Street Gibbon, MN 55335	(Attorney for Debtor) Kurt M. Anderson P O Box 2434 Minneapolis, MN 55402-0434

And I declare, under penalty of perjury, that the foregoing is true and correct.

Dated: August 30, 2004

By /e/ Amy J. Ditty

AJD/ajd#714731v1